

FIRST REGULAR SESSION

HOUSE BILL NO. 575

99TH GENERAL ASSEMBLY

INTRODUCED BY REPRESENTATIVE WIEMANN.

1236H.011

D. ADAM CRUMBLISS, Chief Clerk

AN ACT

To repeal sections 375.1025, 375.1052, 375.1053, and 375.1056, RSMo, and to enact in lieu thereof five new sections relating to internal audit requirements for insurers.

Be it enacted by the General Assembly of the state of Missouri, as follows:

Section A. Sections 375.1025, 375.1052, 375.1053, and 375.1056, RSMo, are repealed
2 and five new sections enacted in lieu thereof, to be known as sections 375.1025, 375.1052,
3 375.1053, 375.1056, and 375.1058 to read as follows:

375.1025. As used in sections 375.1025 to 375.1062, the following terms shall mean:

2 (1) "Accountant" or "independent certified public accountant", an independent certified
3 public accountant or accounting firm in good standing with the American Institute of Certified
4 Public Accountants and in all states in which they are licensed to practice. For Canadian and
5 British companies, it means a Canadian-chartered or British-chartered accountant;

6 (2) "Affiliate" or "affiliated", a person that directly, or indirectly through one or more
7 intermediaries, controls, or is controlled by, or is under common control with, the person
8 specified;

9 (3) "AICPA", the American Institute of Certified Public Accountants;

10 (4) "Audit committee", a committee (or equivalent body) established by the board of
11 directors of an entity for the purpose of overseeing the accounting and financial reporting
12 processes of an insurer or group of insurers, **the internal audit function of any insurer or**
13 **group of insurers (if applicable)**, and **external** audits of financial statements of the insurer or
14 group of insurers. The audit committee of any entity that controls a group of insurers may be
15 deemed to be the audit committee for one or more of such controlled insurers solely for the
16 purposes of sections 375.1025 to 375.1062 at the election of the controlling person. Such

EXPLANATION — Matter enclosed in bold-faced brackets [thus] in the above bill is not enacted and is intended to be omitted from the law. Matter in **bold-face** type in the above bill is proposed language.

17 election shall be exercised under subsection ~~[5]~~ 6 of section 375.1053. If an audit committee is
18 not designated by the insurer, the insurer's entire board of directors shall constitute the audit
19 committee;

20 (5) "Audited financial report", includes those items specified in section 375.1032;

21 (6) "Department", the department of insurance, financial institutions and professional
22 registration;

23 (7) "Director", the director of the department of insurance, financial institutions and
24 professional registration;

25 (8) "Group of insurers", those licensed insurers included in the reporting requirements
26 of sections 382.010 to 382.300, or a set of insurers as identified by management, for the purpose
27 of assessing the effectiveness of internal control over financial reporting;

28 (9) "Indemnification", an agreement of indemnity or a release from liability where the
29 intent or effect is to shift or limit in any manner the potential liability of the person or firm for
30 failure to adhere to applicable auditing or professional standards, whether or not resulting in part
31 from knowing of other misrepresentations made by the insurer or its representatives;

32 (10) "Independent board member", the same meaning as described in subsection ~~[3]~~ 4
33 of section 375.1053;

34 **(11) "Internal audit function", a person or persons that provide independent,**
35 **objective, and reasonable assurance designed to add value and improve an organization's**
36 **operations and accomplish its objectives by bringing a systematic, disciplined approach to**
37 **evaluate and improve the effectiveness of risk management control and governance**
38 **processes;**

39 ~~[(11)]~~ (12) "Insurer", an insurer certified to do business in this state pursuant to section
40 375.161 or 375.831, and to companies authorized to transact business in this state pursuant to
41 chapters 354, 376, 377, 378, 379 and 381;

42 ~~[(12)]~~ (13) "Internal control over financial reporting", a process effected by an entity's
43 board of directors, management and other personnel designed to provide reasonable assurance
44 regarding the reliability of the financial statements, i.e., those items specified in ~~[subsections 2~~
45 ~~to 7]~~ **subdivisions (2) to (6) of subsection 2 and subsection 3** of section 375.1032 and includes
46 those policies and procedures that:

47 (a) Pertain to the maintenance of records that, in reasonable detail, accurately and fairly
48 reflect the transactions and dispositions of assets;

49 (b) Provide reasonable assurance that transactions are recorded as necessary to permit
50 preparation of financial statements, i.e., those items specified in ~~[subsections 2 to 7]~~
51 **subdivisions (2) to (6) of subsection 2 and subsection 3** of section 375.1032, and that receipts

52 and expenditures are being made only in accordance with authorizations of management and
53 directors; and

54 (c) Provide reasonable assurance regarding prevention or timely detection of
55 unauthorized acquisition, use or disposition of assets that could have a material effect on the
56 financial statements, i.e., those items specified in ~~subsections 2 to 7~~ **subdivisions (2) to (6) of**
57 **subsection 2 and subsection 3** of section 375.1032;

58 ~~[(13)]~~ **(14)** "NAIC", the National Association of Insurance Commissioners;

59 ~~[(14)]~~ **(15)** "SEC", the United States Securities and Exchange Commission;

60 ~~[(15)]~~ **(16)** "Section 404", Section 404 of the Sarbanes-Oxley Act of 2002, as amended,
61 and the SEC's rules and regulations promulgated thereunder;

62 ~~[(16)]~~ **(17)** "Section 404 report", management's report on internal control over financial
63 reporting, as defined by the SEC and the related attestation report of the independent certified
64 public accountant as described in subsection 1 of section 375.1030;

65 ~~[(17)]~~ **(18)** "SOX compliant entity", an entity that either is required to be or voluntarily
66 is compliant with all of the following provisions of the Sarbanes-Oxley Act of 2002, as amended:

67 (a) The preapproval requirements of Section 201 (Section 10A(i) of the federal Securities
68 Exchange Act of 1934);

69 (b) The audit committee independence requirements of Section 301 (Section 10A(m)(3)
70 of the federal Securities Exchange Act of 1934); and

71 (c) The internal control over financial reporting requirements of Section 404.

375.1052. 1. Upon written application of any insurer, the director may grant a temporary
2 exemption from compliance with sections 375.1025 to 375.1062 if the director finds, upon
3 review of the application, that compliance with sections 375.1025 to 375.1062 would constitute
4 a financial or organizational hardship upon the insurer. An exemption may be granted at any
5 time and from time to time for a specified period or periods. Within ten days from a denial of
6 an insurer's written request for an exemption from sections 375.1025 to 375.1062, such insurer
7 may request in writing a hearing on its application for an exemption. Such hearing shall be held
8 in accordance with the provisions of chapter 536 pertaining to administrative hearing procedures
9 and shall be a public meeting as provided by subdivision (3) of section 610.010.

10 2. Domestic insurers:

11 (1) Retaining a certified public accountant on August 28, 2009, who qualifies as
12 independent shall comply with sections 375.1025 to 375.1062 for the year ending December 31,
13 2009, and each year thereafter unless the director permits otherwise;

14 (2) Not retaining a certified public accountant on ~~[the effective date of this regulation]~~
15 **August 28, 2009**, who qualifies as independent shall meet the following schedule for compliance
16 with sections 375.1025 to 375.1062 unless the director permits otherwise:

17 (a) As of December 31, 2009, file with the director an audited financial report;

18 (b) For the year ending December 31, 2010, and each year thereafter, such insurers shall
19 file with the director all reports and communications required by sections 375.1025 to 375.1062.

20 3. Foreign insurers shall comply with sections 375.1025 to 375.1062 for the year ending
21 December 31, 1992, and each year thereafter, unless the director permits otherwise.

22 4. The requirements of subsection 3 of section 375.1037 shall be in effect for audits of
23 the year beginning January 1, 2010, and thereafter.

24 5. The requirements of section 375.1053 are to be in effect January 1, 2010. An insurer
25 or group of insurers that is not required to have independent audit committee members or only
26 a majority but not a supermajority of independent audit committee members, because the total
27 written and assumed premium is below the threshold and subsequently becomes subject to one
28 of the independence requirements due to changes in premium shall have one year following the
29 year the threshold is exceeded, but not earlier than January 1, 2010, to comply with the
30 independence requirements. Likewise, an insurer that becomes subject to one of the
31 independence requirements as a result of a business combination shall have one calendar year
32 following the date of acquisition or combination to comply with the independence requirements.

33 6. The requirements of sections 375.1038, 375.1054, and 375.1056 are effective
34 beginning with the reporting period ending December 31, 2010, and each year thereafter. An
35 insurer or group of insurers that is not required to file a report because the total written premium
36 is below the threshold and subsequently becomes subject to the reporting requirements shall have
37 two years following the year the threshold is exceeded to file a report. Likewise, an insurer
38 acquired in a business combination shall have two calendar years following the date of
39 acquisition or combination to comply with the reporting requirements.

40 **7. The requirements of section 375.1055 are effective beginning January 1, 2018.**
41 **If an insurer or group of insurers that is exempt from section 375.1055 requirements no**
42 **longer qualifies for that exemption, it shall have one year after the year the threshold is**
43 **exceeded to comply with the requirements of section 375.1055.**

375.1053. 1. This section shall not apply to foreign or alien insurers licensed in this state
2 or an insurer that is a SOX compliant entity or a direct or indirect wholly owned subsidiary of
3 a SOX compliant entity.

4 2. The audit committee shall be directly responsible for the appointment, compensation,
5 and oversight of the work of any accountant, including resolution of disagreements between
6 management and the accountant regarding financial reporting, for the purpose of preparing or
7 issuing the audited financial report or related work under sections 375.1025 to 375.1062. Each
8 accountant shall report directly to the audit committee.

9 **3. The audit committee of an insurer or group of insurers shall be responsible for**
10 **overseeing the insurer's internal audit function and granting the person or persons**
11 **performing the internal audit function suitable authority and resources to fulfill their**
12 **responsibilities if required by section 375.1055.**

13 ~~[3-]~~ 4. Each member of the audit committee shall be a member of the board of directors
14 of the insurer or a member of the board of directors of an entity elected under subsection ~~[6]~~ 7
15 of this section and subdivision ~~[(6)]~~ (4) of section 375.1025.

16 ~~[4-]~~ 5. In order to be considered independent for purposes of this section, a member of
17 the audit committee shall not, other than in his or her capacity as a member of the audit
18 committee, the board of directors, or any other board committee, accept any consulting, advisory,
19 or other compensatory fee from the entity or be an affiliated person of the entity or any subsidiary
20 thereof. However, if law requires board participation by otherwise nonindependent members,
21 such law shall prevail and such members may participate in the audit committee and be
22 designated as independent for audit committee purposes, unless they are an officer or employee
23 of the insurer or one of its affiliates.

24 ~~[5-]~~ 6. If a member of the audit committee ceases to be independent for reasons outside
25 the member's reasonable control, that person, with notice by the responsible entity to the state,
26 may remain an audit committee member of the responsible entity until the earlier of the next
27 annual meeting of the responsible entity or one year from the occurrence of the event that caused
28 the member to be no longer independent.

29 ~~[6-]~~ 7. To exercise the election of the controlling person to designate the audit committee
30 for purposes of sections 375.1025 to 375.1062, the ultimate controlling person shall provide
31 written notice to the chief state insurance regulatory officials of the affected insurers.
32 Notification shall be made timely prior to the issuance of the statutory audit report and include
33 a description of the basis for the election. The election can be changed through notice to the
34 director by the insurer, which shall include a description of the basis for the change. The election
35 shall remain in effect for perpetuity, until rescinded.

36 ~~[7-]~~ 8. (1) The audit committee shall require the accountant that performs for an insurer
37 any audit required by sections 375.1025 to 375.1062 to timely report to the audit committee in
38 accordance with the requirements of the auditing profession, including:

39 (a) All significant accounting policies and material permitted practices;

40 (b) All material alternative treatments of financial information within statutory
41 accounting principles that have been discussed with management officials of the insurer,
42 ramifications of the use of the alternative disclosures and treatments, and the treatment preferred
43 by the accountant; and

44 (c) Other material written communications between the accountant and the management
45 of the insurer, such as any management letter or schedule of unadjusted differences.

46 (2) If an insurer is a member of an insurance holding company system, the reports
47 required by subdivision (1) of this subsection may be provided to the audit committee on an
48 aggregate basis for insurers in the holding company system; provided that any substantial
49 differences among insurers in the system are identified to the audit committee.

50 [8:] 9. The proportion of independent audit committee members shall meet or exceed the
51 following criteria:

52 (1) If the insurer wrote direct and assumed premiums of zero to three hundred million
53 dollars during the prior calendar year, no minimum requirements are required regarding the
54 number or proportion of audit committee members who shall be independent;

55 (2) If the insurer wrote direct and assumed premiums of three hundred million to five
56 hundred million dollars during the prior calendar year, at least a majority of the members of the
57 audit committee shall be independent; and

58 (3) If the insurer wrote direct and assumed premiums of five hundred million dollars or
59 more during the prior calendar year, a supermajority of at least seventy-five percent of the
60 members of the audit committee shall be independent.

61 [9:] 10. An insurer with direct written and assumed premium, excluding premiums
62 reinsured with the Federal Crop Insurance Corporation and Federal Flood Program, less than five
63 hundred million dollars may make application to the director for a waiver from the requirements
64 of this section based upon hardship. The insurer shall file, with its annual statement filing, the
65 approval for relief from this section with the states that it is licensed in or doing business in and
66 the NAIC. If the nondomestic state accepts electronic filing with the NAIC, the insurer shall file
67 the approval in an electronic format acceptable to the NAIC.

375.1056. 1. Every insurer required to file an audited financial report under sections
2 375.1025 to 375.1062 that has annual direct written and assumed premiums, excluding premiums
3 reinsured with the Federal Crop Insurance Corporation and Federal Flood Program, of five
4 hundred million dollars or more shall prepare a report of the insurer's or group of insurers'
5 internal control over financial reporting, as such terms are defined in section 375.1025. The
6 report shall be filed with the director along with the communication of internal control-related
7 matters noted in an audit described under section 375.1047. Management's report of internal
8 control over financial reporting shall be as of December thirty-first immediately preceding.

9 2. Notwithstanding the premium threshold in subsection 1 of this section, the director
10 may require an insurer to file management's report of internal control over financial reporting if
11 the insurer is in any RBC level event, or meets any one or more of the standards of an insurer

12 deemed to be in hazardous financial condition as defined in ~~[rules adopted by the director]~~
13 **section 375.539.**

14 3. An insurer or a group of insurers that is:

15 (1) Directly subject to Section 404;

16 (2) Part of a holding company system whose parent is directly subject to Section 404;

17 (3) Not directly subject to Section 404 but is a SOX compliant entity; or

18 (4) A member of a holding company system whose parent is not directly subject to
19 Section 404 but is a SOX compliant entity may file its or its parent's Section 404 report and an
20 addendum in satisfaction of the requirement of this section, provided that those internal controls
21 of the insurer or group of insurers having a material impact on the preparation of the insurer's or
22 group of insurers' audited statutory financial statements, namely those items included in
23 subdivisions (2) to (6) of subsection 2 **and subsection 3** of section 375.1032, were included in
24 the scope of the Section 404 report. The addendum shall be a positive statement by management
25 that there are no material processes with respect to the preparation of the insurer's or group of
26 insurers' audited statutory financial statements excluded from the Section 404 report. If there are
27 internal controls of the insurer or group of insurers that have a material impact on the preparation
28 of the insurer's or group of insurers' audited statutory financial statements and those internal
29 controls were not included in the scope of the Section 404 report, the insurer or group of insurers
30 may either file a report under this section, or the Section 404 report and a report under this
31 section for those internal controls that have a material impact on the preparation of the insurer's
32 or group of insurers' audited statutory financial statements not covered by the Section 404 report.

33 4. Management's report of internal control over financial reporting shall include:

34 (1) A statement that management is responsible for establishing and maintaining
35 adequate internal control over financial reporting;

36 (2) A statement that management has established internal control over financial reporting
37 and an assertion, to the best of management's knowledge and belief, after diligent inquiry, as to
38 whether its internal control over financial reporting is effective to provide reasonable assurance
39 regarding the reliability of financial statements in accordance with statutory accounting
40 principles;

41 (3) A statement that briefly describes the approach or processes by which management
42 evaluated the effectiveness of its internal control over financial reporting;

43 (4) A statement that briefly describes the scope of work that is included and whether any
44 internal controls were excluded;

45 (5) Disclosure of any unremediated material weaknesses in the internal control over
46 financial reporting identified by management as of December thirty-first immediately preceding.
47 Management is not permitted to conclude that the internal control over financial reporting is

48 effective to provide reasonable assurance regarding the reliability of financial statements in
49 accordance with statutory accounting principles if there is one or more unremediated material
50 weaknesses in its internal control over financial reporting;

51 (6) A statement regarding the inherent limitations of internal control systems; and

52 (7) Signatures of the chief executive officer and the chief financial officer, or the
53 equivalent position or title.

54 5. Management shall document and make available upon financial condition examination
55 the basis upon which its assertions required in subsection 4 of this section are made.
56 Management may base its assertions, in part, upon its review, monitoring and testing of internal
57 controls undertaken in the normal course of its activities. Management shall have discretion as
58 to the nature of the internal control framework used, and the nature and extent of documentation,
59 in order to make its assertion in a cost-effective manner and, as such, may include assembly of
60 or reference to existing documentation. Management's report on internal control over financial
61 reporting, required by subsection 1 of this section, and any documentation provided in support
62 thereof during the course of a financial condition examination, shall be kept confidential by the
63 department.

64 6. No officer responsible for financial reporting may be a member of the audit
65 committee.

**375.1058. 1. An insurer is exempt from the requirements of sections 375.1025 to
2 375.1062 if:**

3 (1) The insurer has annual direct written and unaffiliated assumed premium,
4 including international direct and assumed premium but excluding premiums reinsured
5 with the Federal Crop Insurance Corporation and Federal Flood Program, totaling less
6 than five hundred million dollars; and

7 (2) The insurer is a member of a group of insurers that has annual direct written
8 and unaffiliated assumed premium, including international direct and assumed premium
9 but excluding premiums reinsured with the Federal Crop Insurance Corporation and
10 Federal Flood Program, totaling less than one billion dollars.

11 2. The insurer or group of insurers shall establish an internal audit function
12 providing independent, objective, and reasonable assurance to the audit committee and
13 insurer management regarding the insurer's governance, risk management, and internal
14 controls. This assurance shall be provided by performing general and specific audits,
15 reviews, and tests and by employing other techniques deemed necessary to protect assets,
16 evaluate control effectiveness and efficiency, and evaluate compliance with policies and
17 regulations.

18 **3. In order to ensure that internal auditors remain objective, the internal audit**
19 **function must be organizationally independent. Specifically, the internal audit function**
20 **shall not defer ultimate judgment on audit matters to others and shall appoint an**
21 **individual to head the internal audit function who will have direct and unrestricted access**
22 **to the board of directors. Organizational independence does not preclude dual-reporting**
23 **relationships.**

24 **4. The head of the internal audit function shall report to the audit committee**
25 **regularly, but no less than annually, on the periodic audit plan, factors that may adversely**
26 **impact the internal audit function's independence or effectiveness, material findings from**
27 **completed audits, and the appropriateness of corrective actions implemented by**
28 **management as a result of audit findings.**

29 **5. If an insurer is a member of an insurance holding company system or included**
30 **in a group of insurers, the insurer may satisfy the internal audit function requirements set**
31 **forth in this section at the ultimate controlling parent level, an intermediate holding**
32 **company level, or the individual legal entity level.**

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